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August 20, 2002

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Ms. Marlene Dortch
Secretary
Federal Communications Commission
445 12th St., SW, Room TWB-204
Washington, DC 20554

Re: Notice of Ex Parte Contact:

In the Matter of Verizon's Petition for Emergency Declaratory and Other Relief, WC Docket No. 02-202

Dear Ms. Dortch:

On Monday August 19, 2002, Michael Del Casino and I met with Matthew Brill, Commissioner Abernathy's Legal Adviser, regarding the above referenced proceeding. In that meeting, we reiterated AT&T's opposition to Verizon's Petition application for all of the reasons articulated by AT&T in its Opposition a copy of which is attached hereto.

Two copies of this Notice are being submitted in accordance with the Commission's rules.

Sincerely,

Robert W. Quinn Jr.

Enclosure
cc: Matthew Brill

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of	)	
	)	
Petition for Emergency Declaratory and Other Relief	)	**WC Docket No. 02-202**
	)	

OPPOSITION OF AT&T CORP.

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August 15, 2002

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FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
Petition for Emergency Declaratory and Other Relief	)	**WC Docket No. 02-202**

OPPOSITION OF AT&T CORP.

Pursuant to the Commission's Notice,[1] AT&T Corp. ("AT&T") submits this opposition to Verizon's Petition[2] seeking (i) broad discretion to demand security deposits and advance payments and otherwise to impose substantial and unwarranted costs on interexchange carriers ("IXC") that pose no exceptional credit risk, and (ii) sweeping Commission pronouncements on incumbent LECs' rights in access customers' bankruptcy proceedings.

INTRODUCTION AND SUMMARY

Verizon's Petition is the latest in a series of anticompetitive attempts by incumbent LECs to leverage the recent bankruptcy filings of several competitive local and long distance carriers to gain regulatory approval for radical new tariff provisions that would substantially disadvantage the remaining competitive carriers that have sound credit and that pose no exceptional bad debt threat. These proposals are justified, Verizon and the incumbent LECs claim, to limit the "financial fallout" from the "difficulties" in the telecommunications industry and thereby to

[1] *See* Wireline Competition Bureau Seeks Comment on Verizon's Petition for Emergency Declaratory And Other Relief, *Petition for Emergency Declaratory And Other Relief*, WC Docket No. 02-202 (released July 31, 2002) ("Notice").

[2] *See* Petition for Emergency Declaratory And Other Relief, *Petition for Emergency Declaratory And Other Relief*, WC Docket No. (filed July 24, 2002) ("Petition").

insure that "surviving carriers" – specifically, the incumbent LECs – will continue to reap additional profits from access services. Petition at 1. And Verizon's Petition claims that in addition to approving changes to its tariffs, the Commission also should act to stem any incumbent LEC losses by issuing broad pronouncements to the bankruptcy courts to ensure that incumbents obtain preferred rights. Verizon's Petition is an incredibly overbroad response to a bad debt problem the incumbents have grossly exaggerated, and should be promptly rejected.

First, although the financial difficulties of certain telecommunications companies cannot be doubted, the assertion of Verizon and other incumbent LECs that the proper response to that problem is to allow those companies with bottleneck facilities to impose *more onerous* payment terms on *all* of their captive access customers is preposterous. Indeed, given the grossly excessive returns the large incumbent LECs achieve on access services, Verizon's plea for expedited relief is simply thinly disguised greed. In 2001, a period in which the incumbent LECs claim that their bad debt uncollectibles rose significantly, each of the large incumbent LECs nonetheless achieved rates of return on special access services of between *21 and 55 percent.* And in 2001 *all* of the large ILECs earned far more than their traditional authorized rate of return on access services as a whole – between 17 and 22 percent, levels that are *even higher* than their average rates of return over the previous four years. Given the hefty margins on services for which incumbents continue to enjoy near monopolies, there is no need for the Commission to take additional steps to insure that incumbents are guaranteed the ability to collect access revenues.

Further, Verizon and the incumbent LECs have also grossly exaggerated their claims that the recent downturn in the market has exposed incumbents to substantial liability from unpaid access bills. Any incumbent LEC bad debt "emergency" conjured up by Verizon and other incumbent LECs is a fiction. The ARMIS data reported by Verizon and other incumbent LECs confirm that they have very low levels of bad debt – generally less than one percent. Indeed, the Commission's existing prescribed tariff language already fully protects Verizon and other LECs from customers with a proven history of non-payment, and from customers without established credit. Verizon and the other incumbent LECs have failed to explain why these provisions, which were in place in prior economic downturns, are no longer sufficient.

But even if Verizon and the incumbent LECs had demonstrated some limited increase in their exposure that is not already appropriately covered by the Commission's longstanding tariff prescriptions relating to non-payment risks, Verizon's petition is by no means a narrowly circumscribed and measured response to any such problem. Rather, it is an incredibly broad and overreaching proposal that not only seeks to pre-arrange a preferred position for the incumbent LECs in bankruptcy proceedings, but also would result in fundamental changes to the access service markets that affect *all* access customers – both financially troubled and healthy carriers.

As the recent tariff filings of Verizon and other LECs demonstrate, the relief requested in Verizon's Petition would be used by incumbent LECs to demand, at their discretion, that virtually every IXC pay them a large security deposit or advance payment. For large IXCs, these amounts could be hundreds of millions of dollars – easily enough to disrupt the business plans of even large carriers that are otherwise able to pay access bills. And even though Verizon asserts that it is interested in "ensuring continuity of service," Petition at 1, Verizon and other LECs have also proposed tariffs that would substantially accelerate the time in which LECs can cut off an IXC's access service, and thus create greater risks of service interruptions (or at least provide incumbent LECs with greater leverage in negotiations to threaten such interruptions). And none of the tariff provisions Verizon is seeking to add would come into play when a carrier actually files for bankruptcy and debt payment terms become subject to the Bankruptcy Code. The additional tariff provisions sought by Verizon and other incumbent LECs, therefore, would primarily impose additional burdens on customers with a *proven credit history* that have continued responsibly to pay their bills. Moreover, these proposed revisions would provide incumbent LECs with a powerful and anticompetitive weapon that they could use to favor affiliated IXCs and to disadvantage their rivals by insisting that rivals provide tens or even hundreds of millions of dollars in cash (or its equivalent), even where the IXC has never missed an access payment and presents no extraordinary risk of nonpayment for the future. The Commission has properly suspended these incumbent LEC tariffs because those tariffs contradict the Commission's prescribed tariff language, and because the LECs failed to show that a waiver of that prescribed language is necessary.

Verizon's Petition seeks to circumvent these impediments to implementing new and anticompetitive tariff provisions by seeking to have the Commission abandon the field, ignore nearly two decades of experience, and allow the LECs unfettered discretion to decide payment terms of their captive customers. But Verizon also has made no showing that drastic changes to the Commission's prescribed tariff language are necessary to protect Verizon from its credit worthy customers. To be sure, Verizon and the other LECs should be able to protect themselves from customers that pose serious credit risks. But the solution is not, as Verizon now asks, to give it and other incumbent LECs unbounded discretion to impose virtually any restriction on any customer that they deem to be a "credit risk." Rather, the Commission's carefully crafted prescribed tariff language remains clearly sufficient to protect LECs from the ongoing "crisis" while protecting customers from dominant LEC-imposed anticompetitive restrictions.

Finally, not content with asking the Commission permission to exploit its bill paying customers, Verizon also asks the Commission to declare that Verizon and other LECs should enjoy preferred rights in bankruptcy. In particular, Verizon contends that, because of the ongoing "crisis," it needs immediate action from the Commission to ensure that it is provided with assurance of payment when it provides telecommunications services to debtors and that existing interconnection contracts are "cured" when they are assigned from a debtor-carrier to a new carrier. But the Bankruptcy Code provides these protections. Thus, it is clear that what Verizon wants is for the Commission to instruct the bankruptcy court as to how these provisions should be applied in practice. Even if the Commission were entrusted with implementing the Bankruptcy Code, the respective rights of creditors and debtors in these contexts must be decided on the "unique facts" of each case, and cannot be declared in the abstract, as Verizon urges. *See In re George C. Frye Co.*, 7 B.R. 856, 858 (Bkrtcy. D. Me. 1980). This is not to say that the Commission should refrain from intervening in bankruptcy proceedings, where appropriate, in order to assist the bankruptcy court in understanding federal telecommunications law and policy. But it would be unwise, and ultimately unsuccessful, for the Commission to attempt to lecture the bankruptcy courts with generic pronouncements about necessarily fact-bound bankruptcy inquiries.

I. VERIZON'S PROPOSAL TO GAIN UNFETTERED ABILITY TO IMPOSE HUNDREDS OF MILLIONS OF DOLLARS OF COSTS ON ITS COMPETITORS MUST BE REJECTED.

Recent LEC attempts unilaterally to alter their tariffs and implement numerous new security deposit/advance payment and other anticompetitive tariff provisions have properly triggered suspension orders (or voluntary LEC deferrals to avoid such orders).[3] Verizon has filed this Petition seeking a declaratory ruling that would give Verizon and other LECs unfettered discretion to implement these and similar changes in future tariffs without fear of additional Commission suspension and investigation orders. As demonstrated below, Verizon's petition must be denied because (1) incumbent LECs' own data refute any claim that new tariff revisions are necessary to protect incumbent LECs' from a bad debt "emergency;" (2) Verizon has failed to provide any other legitimate evidence that the Commission's existing prescribed tariff language is inadequate; and (3) in particular, provisions that have been proposed by Verizon and other dominant LECs are plainly unjust, unreasonable and anticompetitive.

A. There Is No Incumbent Bad Debt "Crisis."

Existing Commission-prescribed tariff provisions already permit LECs to collect large security deposits from customers with a proven history of late payments or with no established credit, and to disconnect those customers' service if they continue to default on bills.[4] Furthermore, bankruptcy laws provide incumbent LECs adequate assurance of payment and

[3] *See, e.g.,* Order, *In the Matter of BellSouth Telecommunications, Inc. Tariff FCC No. 1.*, Transmittal No. 657 (rel. August 2, 2002); Order, *In the Matter of Iowa Telecomm. Serv. Inc. Tariff FCC No. 1.*, Transmittal No. 22. (rel. July 17, 2002); *see also* SBC Transmittals Nos 20, 1312, 2906, 772, and 77 (filed August 2, 2002); Verizon Transmittal No 226 (filed July 25, 2002).

[4] *See* Investigation of Access and Divestiture Related Tariffs, 97 F.C.C.2d 1082, 1168-70 (1984) (emphasis added) ("*1984 Access Tariff Order*").

other remedies against bankrupt customers.[5] Verizon's proposed tariff changes, therefore, are not aimed at deadbeat or bankrupt customers, but rather at healthy customers – which also happen to be Verizon's competitors. And therein lies a fatal flaw in Verizon's Petition. Verizon has not even attempted to show that radical changes to the Commission's prescribed tariff language are required to protect it from the possibility that its credit worthy customers will not pay, or that those customers are not likely to pay their bills in the future. For this reason alone, Verizon's Petition should be denied.

But even lumping all of Verizon's paying, non-paying and bankrupt customers together, the bad debt "emergency" conjured by Verizon and other incumbent LECs does not exist. The LECs' own data (contained in ARMIS 43-01 reports) confirms that, notwithstanding the recent industry downturn, Verizon and other LECs continue to have very low levels of bad debt expenses. For example, Verizon's uncollectibles for both special and switched access services averaged less than *one and a half percent* of revenues in 2001, an extraordinarily low level of bad debt expense.[6] Other LECs are experiencing similar success in collecting on their access bills, with many large incumbents at less than one percent.[7] And even if the LECs' bad debt experience were much worse, the LECs could hardly claim that the industry downturn has had any serious impact on their bottom line. According to Commission's ARMIS data, in 2001, the large incumbent LECs' overall rates of return on access services ranged from 17 percent to as high as 22 percent – far exceeding their traditional authorized rate of return and higher in

[5] *See* 11 U.S.C. § 366. *See also infra* Part II.

[6] *See* 2000 & 2001 ARMIS 43-01, Table I, Cost and Revenue Table, Special Access & Traffic Sensitive: Total, Columns (r), (s), Network Access Services, Row 1020 & Uncollectibles, Row 1060.

[7] *Id.* (for example, Qwest's data shows a 0.72% rate; Pacific Bell, a 0.25% rate, and Ameritech, a 0.11% rate)

virtually all cases than the rates of return in the previous four years.[8] And these ILECs' rates of return for special access are as high as *55 percent* in 2001 – and each large incumbent LEC has achieved significant increases in their rate of return for special access in each year since 1996.[9] And their earnings for switched access (including common line) have also been exorbitant since 1996.[10] Verizon's claims that draconian measures are required to protect it and other LECs from non-payment of access bills are therefore entirely baseless.

Not surprisingly, Verizon has in other related pleadings urged the Commission to ignore these facts, and focus instead on the fact that Verizon's 2001 uncollectibles are, in some instances, higher than its 2000 uncollectibles.[11] However, an honest review of those numbers shows that, even with those increases, the level of uncollectibles experienced by Verizon are quite low. In 2000, Verizon's ARMIS 43-01 reports show that its special access uncollectibles for Verizon-South, Verizon-North, and Verizon-GTE were 0.45%, 0.70%, and 0.49%, respectively. In 2001, those numbers were still minute, totaling 0.58%, 2.89%, and 0.66%, respectively. *ARMIS Uncollectible Data.* Thus, although Verizon's uncollectibles rose from 2000 to 2001, the absolute level of Verizon's uncollectibles are hardly at levels requiring radical Commission action that would impose massive new costs on Verizon's customers (and

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[8] *See* 1997-2001 ARMIS 43-01, Table I. Cost and Revenue Table, Interstate, Column (h), Average Net Investment, Net Return, Rows 1910, 1915.

[9] *See* 1997-2001 ARMIS 43-01, Table I. Cost and Revenue Table, Special Access, Column (s), Average Net Investment, Net Return, Rows 1910, 1915.

[10] *See* 1997-2001 ARMIS 43-01, Table I. Cost and Revenue Table, Traffic Sensitive, Column (r), Common Line, column (m), Average Net Investment, Net Return, Rows 1910, 1915.

[11] *See* Reply Comments Of Verizon To Petitions To Reject Or Suspend And Investigate, *Verizon Telephone Companies Tariff FCC Nos. 1, 11, 14 and 16, Transmittal No. 226*, at 2-3 (filed August 7, 2002) ("Verizon Tariff Reply").

competitors) that have been and are paying their bills.[12] Accordingly, the Commission should, as it has done in the past, reject Verizon's and other LECs' attempts to take advantage of a dip in the business cycle to obtain anticompetitive tariff discretion.

Indeed, Verizon is well aware that current market conditions do not support a radical departure from prior Commission rules. In a blatant attempt to overcome the existing market statistics, and to justify imposing massive new security deposit/advance payment restrictions on its *paying* customers, Verizon says that, unless it is granted the protections that it is seeking in the Petition, it and its sister LEC monopolists will be "dragged under" by the imminent collapse of the competitive carriers, including the "demise of many leveraged, resale-based carriers . . . [and] even larger carriers with significant capital investment in their own facilities." Petition at 3. This claim is utter nonsense. Those predictions are predicated on the baseless claim that the pro-competitive provisions of the Telecommunications Act and the Commission's rules encouraged unsustainable competitive entry. In reality, the Telecommunications Act and the Commission rules provide, for the most part, the necessary framework to allow local and long-distance telephone competition to flourish. To be sure, Verizon and the other LECs have consistently resisted and undermined the competition-enhancing provisions of the Act and the Commission's rules – actions which have contributed, in no small measure, to the financial difficulties currently faced by some carriers. To allow the LECs to use this problem of their own

[12] Verizon's argument also ignores the fact that its uncollectibles naturally fluctuate from year-to-year, sometimes increasing and sometimes decreasing. For example, Verizon's uncollectibles actually fell from year-to-year between 1995 and 1997. *See* Verizon Tariff Reply, Exhibit B. Yet Verizon's proposed tariff revisions do not even contain provisions that would remove the new security deposit and accelerated disconnect terms in the future when uncollectibles begin to move back towards zero, from their current levels of less than one percent (although a modification in this regard would do nothing to ameliorate the other glaring discriminatory aspects of its proposed tariff).

making as a means of further exploiting their bottleneck facilities would stand fairness on its head.

B. Verizon Has Not Provided Sufficient Evidence To Support A Reversal Of Longstanding Commission Precedent That Strictly Limits Deposit And Termination Of Service Provisions.

Even if Verizon could demonstrate that its uncollectibles had risen to a substantial level, and that its proposed remedy were aimed at carriers that are not paying their bills, Verizon has still failed to justify its Petition. In fact, Verizon has not even described the specific relief its "emergency" Petition seeks. Rather, Verizon simply asserts that the Commission should declare that dominant LECs are generally permitted to "revise . . . tariffs to require advanced payments, security deposits, and shorter notice periods where necessary to ensure adequate assurance of payment by their customers." Petition at 3. As evidenced by the tariff changes that Verizon and the other LECs have filed to date, it is clear that dominant LECs would use this unfettered authority to implement tariff terms that are unreasonable, discriminatory and anticompetitive.

Security Deposits/Advance Payments. The LECs' current tariffs have for over fifteen years permitted them to demand security deposits "*only*" for a narrow class of IXCs: first, those carriers that "ha[ve] a *proven history* of late payments" to the LEC, and second, those carriers that "d[o] not have established credit."[13] The Commission's original prescription of a narrow security deposit requirement was prompted by dominant LEC proposals – strikingly similar to the recent transmittals filed by Verizon and other LECs (which have either been suspended for investigation or voluntarily withdrawn by the LEC) – to give LECs discretion to require deposits from virtually any IXC.[14] The Commission found "several flaws" in the LECs' proposed tariff

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[13] *1984 Access Tariff Order*, 97 F.C.C.2d 1082, 1168-70.

[14] *Id.* at 1168-69.

on security deposits, including the fact that it could be applied selectively to carriers chosen unilaterally by the LEC. The Commission therefore found that the LECs' proposed tariffs were "unreasonably onerous" in scope and had "anticompetitive effects."[15] Accordingly, the Commission determined that those proposed tariffs "*must* be amended" and prescribed the more narrow language limiting security deposits to carriers with a "proven history of late payments" or with "no established credit."[16] The Commission has never suspended or set aside its prescription, and Verizon's Petition offers no legitimate reason for the Commission to do so now.

Despite the Commission's clear findings, Verizon and other LECs did not abandon their effort to demand unwarranted security deposits from other carriers. In each prior instance, the Commission refused to allow the dominant LECs the broad discretion to determine whether their captive customers must provide a security deposit prior to purchasing access services. In 1987, for example, BellSouth sought to revise it tariff to increase (by 50 percent) the deposit that affected IXCs were required to pay BellSouth.[17] BellSouth claimed – as Verizon claims now – that such provisions were necessary because "some IXCs have filed for bankruptcy while owing payments to BellSouth."[18] The Commission, however, rejected that claim, noting that "BellSouth does not adequately identify the need" for its proposed increase and "has not explained why other available measures have been unavailing to avoid the risks" of non-

[15] *Id.*

[16] *Id.*

[17] *See Annual 1987 Access Tariff Filing*, 2 FCC Rcd. 280, 317-18 (1987) ("*1987 Access Tariff Order*").

[18] *Id.* at 304.

payment.[19] Further, the Commission again found that the proposal to increase the security deposit was overbroad, and that any advantages to be gained by BellSouth were "outweighed by the disadvantages to *customers that may not pose a risk to BellSouth*."[20]

In this regard, the Commission's *1987 Access Tariff Order* rejected BellSouth's claim that drastic changes to the Commission's prescribed tariff language were necessary because of a downturn in the economy.[21] The Commission explained that BellSouth failed to submit information "regarding *actual* losses resulting from an *I[X]C's* ultimate failure to pay its bills."[22] Here, as explained above, the case is even weaker. Verizon's own data filed with the Commission show that Verizon is not experiencing substantial (or even moderate) losses do to unpaid bills. Verizon's data show that for 2001 its uncollectibles for special and switched access, as a percentage of revenues for those services, were on average less than 1.5 percent of associated revenues.[23] And Verizon's most recent annual ARMIS data filed with the Commission show that its annual returns from special access exceed *20 percent*.[24] Those massive returns are due in no small part to the fact that Verizon and other LECs have for years leveraged their dominant positions and gamed the Commission's pricing flexibility rules to the detriment of their competitors which, ironically, Verizon now claims are less creditworthy.

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[19] *Id.* at 318.

[20] *Id.* at 318 (emphasis added).

[21] *Id.* at 304, 318.

[22] *Id.* at 304 (emphasis added).

[23] *See* 2000 & 2001 ARMIS 43-01, Table I, Cost and Revenue Table, Special Access & Traffic Sensitive: Total, Columns (r), (s), Network Access Services, Row 1020 & Uncollectibles, Row 1060.

[24] *See* 1997-2001 ARMIS 43-01, Table I. Cost and Revenue Table, Special Access, Column (s), Average Net Investment, Net Return, Rows 1910, 1915.

Verizon also notes that AT&T has from time-to-time insisted on provisions in its contracts with customers that require security deposits and other provisions that protect against default. The critical difference is that, if the customer is not satisfied with the terms AT&T offers or the deposit that AT&T requires, the customer can seek to obtain services from another provider. The customer of a dominant LEC, by contrast, generally has no such choice – which is why the Commission has always recognized the need for prescription in this context that minimizes dominant LEC abuse of security deposit, advance payment and termination requirements.

Termination Provisions. Verizon's proposal also would require the Commission to undo its prescribed tariff language that dominant LECs must use for terminating an access customer's service for nonpayment or failure to comply with other specified tariff conditions. In its *1984 Access Tariff Order*, the Commission rejected a LEC proposal to allow termination of service 20 days after written notice to an access customer that it had committed "any violation of the tariff." 97 F.C.C.2d at 1155. The Commission rejected that proposal as "unreasonable," prescribed a number of changes to the proposed tariff – including language that extended the notice period for termination to 30 days (*id.* at 155-56) – and that prescription has been reflected in dominant tariffs ever since.

Moreover, in its *1987 Access Tariff Order*, the Commission found serious flaws with BellSouth's proposal (made concurrently with its proposal to increase security deposits) to reduce the notice period for termination to 15 days. 2 FCC Rcd. at 304. BellSouth claimed that this revision was necessary to reduce bankruptcy risks. The Commission rejected this rationale, and explained that the reduction in the termination period was "too broad" to "address the potential problems BellSouth has identified." *Id.* That was because the shorter period applied equally to *all* carriers, including those that did "not pose a risk [of non-payment] to BellSouth." *Id.* For those carriers, the proposal to shrink the termination period would be unfairly burdensome and would sharply limit, for example, their "opportunity to review and verify their bills." *Id.* Accordingly, the Commission did not allow dominant LECs the discretion to insist upon shorter notice periods, at least absent both more "adequate documentation" on the actual losses and express limitations in any proposed tariff that "more directly applied *only* to those customers that might default." *Id.* The Commission has not suspended or set aside its 1984 prescription on termination periods, and Verizon has offered no reason for the Commission to do so now.

C. The LECs' Proposed Changes To The Commission's Rules Are Anticompetitive And Unreasonably Discriminatory.

Even if Verizon had provided sufficient evidence that the Commission should change its prescribed tariff language, Verizon's Petition would still have to be denied. To be lawful, a tariff must not only be "just and reasonable" and "non-discriminatory," but also "must contain clear and explicit" language in order "to remove all doubt" as to the proper application of the tariff. *See* 47 U.S.C. §§ 201, 202; 47 C.F.R. § 61.2. The unilateral discretion sought by Verizon's Petition and the type of language that Verizon and other dominant LECs have proposed to implement with that discretion violate both the Act and the Commission's rules.

Security Deposits/Advance Payments. Verizon's Petition seeks to endow all dominant LECs with virtually unlimited discretion to demand security deposits or advance payments from any IXC – authority that these LECs could and would use to discriminate against rival IXCs, to force IXCs to subsidize their local services, and ultimately to weaken these carriers' ability to compete in both local and long distance markets.

The recent transmittals of various dominant LECs amply demonstrate that they have no desire to create limited, specified, and reasonable measures to secure payment from customers who have actually demonstrated, by objective criteria, that they in fact present unusual risks of nonpayment. Rather, these transmittals – though they vary in certain details – are each crafted so that dominant LECs could decide for themselves from which IXC they could demand security deposits and advance payments, on terms that are patently one-sided and anticompetitive.

For example, Verizon's recent transmittal proposed that an IXC must pay Verizon if (1) it "has fallen in arrears on its account balance in any two (2) months out of any consecutive twelve (12) month period" or (2) it "owes $250,000 or more to [Verizon] that is thirty (30) days or more past due"[25] These incredibly broad provisions are in no way "undeniable" signs of financial distress (*cf.* Verizon Transmittal No. 226, D&J at 7) ("Verizon D&J"), and they go far beyond the existing limits that require a "proven history" of non-payment. They could apply, for example, to an IXC that twice in a year had paid less than its full access bills by only *de minimis* amounts (that may themselves be the subject of legitimate billing disputes). Especially given the complexity of the intercarrier billing process, such minor discrepancies are hardly unexpected, and do not provide any justification for a dominant LEC to demand advance payments or deposits that would necessarily be grossly disproportionate to these access bill payment discrepancies. Alternatively, an IXC that was even a single day late (for any reason) with a relatively insubstantial access payment for a given month could be required to forfeit cash – for an entire year – equal to two months worth of access charges. Such conditions are precisely the

[25] Verizon Transmittal No. 226, First Revised Page 2-26 (filed July 25, 2002). SBC proposed a similar trigger, although SBC was audacious enough to suggest that these terms have been in place for years, and that its filing was meant merely to "clarify" the Commission's existing prescription. As AT&T explained however, nothing in the Commission's prescription orders or in the years of implementation of that order justifies SBC's position.

type that "impose significant sanctions" for very "insignificant violations" of a tariff, *1984 Access Tariff Order*, 97 F.C.C.2d at 1155, and are therefore unreasonable.

Contrary to the LECs' claims, these triggers are not the same market-based protections that suppliers in competitive industries can typically impose. Those types of companies generally are not able to insist that their customers provide security deposits or advance payments when they are late (by any amount) with two payments in a given year; rather, they generally charge interest or late fees. And because of the market forces that dominant LECs do not encounter, companies in competitive industries cannot use imprecise and incredibly broad provisions to lump customers with ample ability to pay with those that have a proven history of non-payment. If they did, the financially viable customers would find a new supplier – an option not available to IXCs, which must purchase the LECs' access. Thus, while Verizon has asserted that these revisions are necessary to ensure that "struggling companies do not impose unnecessary harm upon healthy carriers," Verizon D&J at 3, what is in fact necessary is for the Commission to reject Verizon's Petition so that dominant carriers are not able to impose unnecessary harm upon healthy interexchange carriers.

Likewise, some of the dominant LECs' recent tariff revisions would give them the right to demand advance payments and security deposits for customers with senior debt securities that are either "below investment grade" or are "at the lowest investment grade rating category by a nationally recognized statistical rating organization and are put on review for a possible downgrade." *E.g.*, Verizon D&J at 4; *see also* SBC Transmittals, No.77, D&J at 3. These provisions are hopelessly overbroad. AT&T, for example, has recently had its debt ratings downgraded by certain companies, but it has not failed to make a non-disputed access payment to these LECs and poses no serious credit risk to them. Nevertheless, under these transmittals, AT&T (or any other IXC with an exemplary payment history) could be made to provide dominant LECs with substantial deposits or advance payments, simply because one of them may have "concerns" that AT&T's bond rating may be lowered.

Indeed, providing the incumbent LECs with the ability to revise its tariffs in this way would create powerful perverse incentives for these LECs to be less, rather than more, accurate in its access billing to IXCs, or even to engage in intentional overbilling. Faced with an inaccurate or clearly overstated access bill, an IXC would be confronted with the "Hobson's choice" of either paying the excessive access charges or laying itself open to being mulcted by the LECs for an enormous deposit or advance payment, at the peril of having its service almost immediately terminated if it did not accede to the latter demands. There can be no justification for allowing the LECs to implement tariff changes that have such serious untoward consequences.[26]

What is perhaps most troubling about the proposal is that these dominant LECs would almost certainly use any such newly-obtained discretion to discriminate against IXC rivals and in favor of the LECs' own affiliated IXC (or some other favored carrier). Thus, the dominant LECs could rely on these tariff provisions to demand that all IXCs provide significant security deposits/advance payments, but then determine that the LECs' long distance affiliates are sufficiently creditworthy to be excused from such a requirement. Indeed, even if an incumbent LEC required its affiliate to post a deposit or make an advance payment – and in an amount similar to those posted by IXCs – there would still be little hardship on the LEC, because such a

[26] Many of the proposed terms are also patently one-sided in favor of the LEC. SBC, for example, proposed to pay interest on deposits (but *not* an advance payment) at an extremely low interest rate – one that would effectively allow SBC to use the deposits to make money that could subsidize SBC's own operations. The interest rate paid by SBC on these deposits is far less than the rate SBC demands from customers for late payments.

deposit would constitute the classic "left-pocket, right-pocket" transfer. In both cases, the unfettered right to demand a security deposit from any IXC would, as the Commission recognized in 1984, be a powerful anti-competitive and discriminatory weapon.

In addition to the conditions that trigger the large security deposits and prepayments, there are a number of other serious problems with allowing dominant incumbent LECs the ability easily to implement such tariff provisions. First, it is significant that the amount of the deposits that these LECs would demand are very substantial. Indeed, an incumbent LEC could insist that an IXC either make a deposit of up to two months of access charges or make an advance payment for one month of access charges. For a carrier the size of AT&T, these amounts would require AT&T to deposit *hundreds of millions of dollars* with a single incumbent LEC. And, according to the language in these proposed tariffs, these deposits must be paid "in cash" or using credit instruments that are costly and that themselves require significant amounts of cash. There is no reason for most IXCs (*i.e.*, those that have a history of timely payment) to devote scarce cash in order to provide the substantial security deposits that Verizon and other dominant LECs might demand.

Second, some incumbent LECs have proposed that they retain any security deposits for up to one year *after* the conditions that triggered the deposits have ceased to exist. Even if the conditions triggering the deposits were reasonable (which they are not), there is no possible justification for an incumbent LEC to keep any deposits for so long – particularly in light of the fact that these recent proposals would in many cases allow incumbents to retain almost indefinitely a deposit or advance payment once tendered, or at a minimum to immediately demand another deposit if an IXC once again met one of the six specified conditions.[27] But the provisions are particularly draconian because the LECs could demand deposits even from carriers that pose no serious financial risk of non-payment. In that circumstance, these LECs' proposals would require healthy carriers to tie up tens or even hundreds of millions of dollars for no valid reason.

Reduced Termination Provisions. A grant of Verizon's Petition also would allow incumbent LECs to implement their recent unreasonable proposals to reduce dramatically the time in which LECs may terminate access services – in some cases, in as little as just 7 days. These LECs have claimed that the current 30 days is "not necessary to protect the [IXC's] customers," in part because these LECs assert that the 30 days specified in the tariff often occurs "in addition to other mandatory wait periods" or after "negotiations" with the IXC.[28] Even assuming that is true, however, the dominant LECs' tariff revisions would not merely apply in those circumstances, but would apply whenever *any* IXC – even one that presents no payment risks – fails to pay an access bill in full (or to meet one of the other conditions specified in the tariff). The Commission has recognized for many years that such accelerated termination provisions are not reasonable when they apply generally to IXCs that pose no risk. *See 1987 Access Tariff Order* at 304. Such provisions give the dominant LECs far too much leverage in negotiating billing or other disputes with IXCs. The ability to terminate access services so promptly – which would disrupt the long distance services of IXCs' customers – is a powerful

[27] For example, under the tariff revisions proposed by Verizon, it could retain an IXC's deposit or advance payment so long as that access customer's senior debt securities are classified as below investment grade, regardless of how long the IXC makes timely payment of Verizon's access bills in full.

[28] *E.g.*, Verizon D&J at 9; SBC (Pacific) D&J at 11.

threat in the hands of dominant LECs, which could and would be used in a discriminatory fashion.

Moreover, reducing the time for IXCs and other carriers to respond to LECs' claims that bills have not been paid increases the likelihood of service disruptions. The existing 30-day period provides time for carriers and the LECs to work out honest billing and payment errors. The 30-day period also provides carriers with temporary cash shortfalls to address those problems and pay outstanding bills (with interest where appropriate) without disrupting service to carriers' customers. Reducing the termination intervals by more than half would substantially increase the likelihood that service would be terminated in these situations.

Notably, these service disruptions would not be limited to interstate services. Interstate and intrastate traffic are routinely carried over the same lines and switches.[29] To the extent that a LEC "turns off" a carrier's interstate traffic, that carrier's intrastate traffic will be shut down as well. Thus, with regard to switched access services, the restrictions that Verizon and other LECs seek to impose would have a substantial impact on intrastate matters within the exclusive jurisdiction of the states. For that reason, the Commission should consider convening and consulting a Joint State Board before allowing any LEC to institute reduced termination intervals.

[29] In general, inter- and intrastate traffic is calculated for billing purposes. The inter- and intrastate traffic is not physically separated on different lines and switches.

II. THE COMMISSION SHOULD NOT ISSUE THE DECLARATORY RULINGS VERIZON SEEKS REGARDING BANKRUPTCY-RELATED ISSUES AND CUSTOMER TRANSFERS.

A. The Commission Should Not Issue Declaratory Rulings On The Scope of The Rights And Obligations Imposed On Carriers By The Bankruptcy Code.

Verizon also asks the Commission to issue two declaratory rulings that relate to bankruptcy law. *First*, Verizon asks the Commission to establish a policy that it will intervene on behalf of carriers in bankruptcy proceedings and uniformly support carrier's requests for requiring debtors to provide "advance payment" for telecommunications services. More specifically, in its Petition, Verizon claims that because regulators "prevent carriers from terminating service," "creditor carriers are left with no viable means of ensuring payment for service." Petition at 7.

That is false, as Verizon well knows. Under section 366 of the bankruptcy code, 11 U.S.C. § 366, "utilities" are only required to provide service if they are given "adequate assurance" of payment by the debtor. Further, "assurance" will be considered "adequate" only when "*the Court*" – not the debtor – "find[s] that the utility is not subject to an unreasonable risk of future loss." *In re George C. Frye Co.*, 7 B.R. 856 (Bkrtcy. Me. 1980).

Thus, given that the bankruptcy code provides protection for creditor carriers providing services to debtors, Verizon's position must be that the Commission should declare as a matter of federal law that only "advanced payment" is "adequate assurance" within the meaning of 11 U.S.C. § 366 when telecommunications services are involved. *See* Petition at 7. Even if it were in the Commission's purview to opine on the scope of the nation's bankruptcy laws, bankruptcy precedent clearly permits Verizon to obtain, in appropriate circumstances, the very relief that it wants.[30] For example, advanced payments are routinely ordered where the debtor has a history of late and/or inadequate payments or there are questions regarding the debtor's solvency.[31] And it is precisely for those reasons that AT&T agrees with Verizon that WorldCom should be required to make advanced payments as a pre-condition to obtaining telecommunications services. *See* Objections of AT&T Corp., *In Re. WorldCom, Inc.*, Case No. 02-13533 (AJG) (Bkrtcy. S.D.N.Y. Aug. 8, 2002); Objections of Verizon, *In Re. WorldCom, Inc.*, Case No. 02-13533 (AJG) (Bkrtcy. S.D.N.Y. Aug. 8, 2002).

That said, the ultimate form that the "adequate assurance" must take is properly left to the discretion of the bankruptcy court and cannot be specified in advance by the Commission. "Every Section 366(b) proceeding must be decided *upon its unique facts* and the ultimate finding by the Court must be that the utility involved has, or has not been provided with adequate assurance of payment." *In re George C. Frye Co.*, 7 B.R. 856, 858 (Bkrtcy. D. Me. 1980) (emphasis added). Thus, the bankruptcy courts have rejected the claim that a deposit is "required in every case in order to provide adequate assurance of payment." *Id.* Instead, courts have found that where the "estate is sufficiently liquid, the guarantee of an administrative expense priority may constitute adequate assurance of payment for future services." *In re Utica Floor Maintenance, Inc.*, 25 B.R. 1010, 1014 (Bkrtcy. N.D.N.Y. 1982) (quoting H.Rep. No. 95-595,

[30] *See, e.g., Lloyd* v. *Champaign Tel. Co.*, 52 B.R. 653 (Bkrtcy S.D. Ohio 1985); *In re 499 W. Warren Street Associates Ltd. Partnership*, 138 B.R. 363 (Bkrtcy N.D.N.Y. 1991); *In re Cunha*, 1 B.R. 330 (Bkrtcy. Va. 1979); *In re Robmac, Inc.*, 8 B.R. 1 (Bkrtcy. Ga. 1979).

[31] *See, e.g., Lloyd v. Champaign Tel. Co.*, 52 B.R. 653 (Bkrtcy S.D. Ohio 1985); *In re. Sun-Tel Communications, Inc.*, 39 B.R. 10 (Bkrtcy. S. D. Fla. 1984). *See generally Virginia Electric & Power Co. v. Caldor, Inc.*, 117 F.3d 646 (2d Cir. 1997).

95th Cong., 1st Sess. 350 (1977), U.S. Code Cong. & Admin. News 1978, p. 6306); *see also id.* ("It will not be necessary to have a deposit in every case.").[32]

This is not to say that the Commission should hesitate to intervene in bankruptcy proceedings or, when it does so, it should refrain from urging that the court require the debtor to provide advanced payments. To the contrary, in fulfilling its public interest responsibilities, the Commission should actively monitor ongoing bankruptcy proceedings and intervene where appropriate. But given that the bankruptcy code clearly provides carriers with protections when providing telecommunications services to debtors, and given that the form that the protections should take will depend upon the "unique facts" of the case, the Commission should reject Verizon's request that it establish a policy in which it would always urge the bankruptcy court to require advanced payments.

Second, Verizon asks the Commission to issue a declaratory ruling regarding the meaning of 11 U.S.C. § 365, which, according to Verizon, provides that, when a contract entered into by the debtor is assigned to a purchaser, the purchaser becomes liable for any indebtedness under the contract and must provide a cure. Petition at 8-9.[33] Although Verizon suggests that all it wants is a declaration from the Commission that the Communications Act does not override

[32] In *Virginia Electric & Power Co. v. Caldor*, the Second Circuit considered six factors in assessing whether adequate assurance should take the form of a deposit in the context of a debtor purchasing services from a utility. 117 F.3d at 650-651. The six factors it examined were: (1) the debtors' cash on hand and access to debtor-in-possession financing; (2) whether the debtors posed significantly less risk than other customers of the utilities; (3) whether the utilities were better able to monitor the financial strength of the debtors; (4) whether the debtors were solvent and operating out of the proceeds of their businesses; (5) whether the debtors' good prepetition payment history; and (6) whether the utilities required deposits prepetition. *See id.*

[33] Verizon misstates the Code. Section 365(b)(1)(A) makes clear that is "the trustee" that must "cur[e]" (or provide assurances that it will promptly cure) any default in a contract. 11 U.S.C § 365(b)(1)(A). The obligations of any assignee of a debtor's contract are found in Section 365(f)(2), which provides that a debtor's contract may be assigned only if the trustee assumes the contract and the assignee provides "adequate assurance of future performance." *Id.* § 365(f)(2).

section 365's general requirement that a party must provide adequate assurance of future performance of a contract when it steps into the debtor's shoes under that contract, Petition at 8, read in context, Verizon asks the Commission to make a far more sweeping pronouncement regarding the scope of the bankruptcy laws.

In particular, Verizon appears to be renewing arguments it has made in the context of the Winstar bankruptcy proceeding regarding whether carriers are obligated under 11 U.S.C. § 365 to assume and cure the interconnection agreements entered into by debtor. *Compare* Petition at 9 *with* Comments and Counter-Petition of Verizon, WC Docket No. 02-80 (filed Apr. 29, 2002). In the Winstar bankruptcy proceeding, Verizon has contended that, despite the facts that i) Winstar has rejected its interconnection agreements with Verizon and transferred its customers to IDT and ii) IDT has requested "new" service in its own name, IDT must assume and cure Winstar's existing contracts with Verizon because all that has occurred is a mere "name change." *Id.* at 3. Thus, Verizon urges the Commission to declare that, where a "new" carrier seeks to serve customers of a debtor carrier using the same circuits, the new carrier has *in fact* assumed the debtor's underlying service agreements for purposes of 11 U.S.C. § 365 and, therefore, must cure any outstanding debts. *See* Petition at 9 ("[I]f a carrier wishes to receive the benefit of the debtor's pre-existing service arrangements without the burden and potential delay of ordering its own replacement facilities, the carrier should be considered to have *taken an assignment for purposes of bankruptcy law* and the assignee must assume the outstanding indebtedness and negotiate a cure.") (emphasis added).

The Commission should squarely reject Verizon's request to opine in the abstract as to when a party has, or has not, "taken an assignment for purposes of bankruptcy law" in this (or any) context. Although, as Verizon notes, the Commission should "harmonize" its policies with those of the Bankruptcy Code, it is the bankruptcy court, not the Commission, that is entrusted with implementing the Code's provisions. On a practical level, whether a party has unlawfully avoided any of section 365's requirements cannot be answered in the abstract. Rather, it must be determined case-by-case on the basis of the relevant facts. The only entity in the position to undertake such a determination, of course, is the bankruptcy court, which will have all the relevant parties before it and the ability to develop the necessary record evidence to make the determination.

B. The Commission Should Reject Verizon's Attempts To Interject Itself In The Migration Of Customers Between Competitive Carriers.

Lastly, Verizon asks the Commission to issue a declaratory ruling with regard to coordination of the transfer of customer bases between carriers. Petition at 10-11. It is, however, far from clear what relief Verizon is in fact seeking. Verizon claims that it asks only that a single carrier be designated for coordinating end-user transfers with incumbent LECs in the context of mass migrations, *id.* at 11, but it also asks the Commission to modify its discontinuance rules that govern discontinuance notification to customers and regulators. *Id.* at 11 n.4.

In all events, the rule proposed by Verizon is unnecessary and is predicated on Verizon's baseless claims regarding the "centrality" of incumbent LECs' role in the migration of customers between competitive carriers. The entirety of the "support" for the requested relief consists of Verizon's bare assertions regarding the potential for stranded plant. Petition at 10. Although this claim should now be familiar to the Commission because of the frequency at which the incumbents repeat it, they continue to provide no support for it.

Further, the appropriate scope of the incumbent's role in the migration of customers between competitive carriers is generally quite limited. Incumbents play no role in transfer of customers between facilities-based providers. And with regarding to carriers using UNEs to serve local customers, little or no additional provisioning is generally required in the case of a transfer between competitive carriers.

To be sure, in the case of migration of customers involving UNE-based carriers, either the selling or acquiring carrier must notify the incumbent of the transfer so that the incumbent can make the necessary billing changes. But there is clearly no need for the Commission to specify which carrier should be the one to provide the incumbent with the necessary information. Certainly, Verizon has provided no evidence that this information will not be provided by carriers that have every incentive to ensure that the incumbent is given no opportunity to interfere with the customer transfer process.[34]

Finally, the Commission must recognize in this context the anticompetitive potential of increasing the role of incumbent LECs in the transfer of customers between competitive carriers. Incumbent LECs have both the incentive and ability to abuse their role in order to impede the transfer and "winback" those customers. For example, as AT&T has previously described, certain LECs have availed themselves of opportunities to facilitate the transfer customers in ways that cause customer confusion and that provide the LEC with an unfair opportunity to promote its services and those of its affiliates. Thus, when thousands of customers were transferred to AT&T's underlying network services by IDT, a switchless reseller, in the wake of Global Crossing's bankruptcy, SBC played a message to transferred customers that suggested that the customers had in fact been "slammed," and encouraged the end users to contact SBC. That message, which was generated automatically because the underlying CIC code changed,

[34] Moreover, proceedings at the state and even the federal level have been convened to address a number of customer migration issues. There is no basis to grant Verizon's request for an FCC directive that could conflict with these proceedings, which generally provide an opportunity for input from all parties about the feasibility and financial impact of specific notice requirements.

could only cause customer confusion – which would in fact generate incoming calls to SBC operations, which SBC would no doubt use to engage in cross-selling of its local and long distance services. Accordingly, the Commission should not issue a broad declaratory ruling that would result in customer confusion and additional opportunities for incumbent LECs to promote themselves.

CONCLUSION

For the foregoing reasons, the Commission should reject Verizon's Petition.

Respectfully submitted,

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August 15, 2002

CERTIFICATE OF SERVICE

I hereby certify that on this 15th day of August, 2002, I caused true and correct copies of the forgoing Petition of AT&T Corp. to be served on all parties by mailing, postage prepaid to their addresses listed on the following service list.

Dated: August 15, 2002
Washington, D.C.

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